



Fitch Downgrades Avianca Holdings to 'RD'

Fitch Ratings-Chicago-22 July 2019: Fitch Ratings has downgraded Avianca Holdings' Long-Term Foreign and Local Currency Issuer Default Rating (IDR) to 'RD' from 'B-'. The ratings have been removed from Rating Watch Negative. A full list of rating actions follows at the end of this release.

This downgrade follows the announcement by Avianca that it has deferred payments on certain long-term leases and on payment of principal on certain loan obligations. This is in line with the definition of restricted payment (RD) in accordance with Fitch's criteria. Avianca has announced a debt restructuring plan, which also includes the announcement of an exchange offer of its 8.375% outstanding senior notes due 2020 for new notes with the same terms as the existing notes, yet, with the addition of security. The new notes will mature in May 2023, carry an interest of 9.00% and be subject to new investment or financing of USD250 million and approval of the debt refinancing.

KEY RATING DRIVERS

Debt Restructuring: This announcement of payment deferrals and a debt restructuring with its creditors indicates a default-like process, which is commensurate with a rating of 'RD'. Avianca is current on its interest payments, and intends to resume scheduled principal payments once these agreements have been successfully reached. The company aims to have all creditors to be paid in full, including principal and interest. Part of the debt restructuring considers the receivable of previously announced investment into Avianca by United Airlines, Inc. and Kingsland Holdings Limited, in a total amount of USD250 million.

Notes Exchange on Secured Basis: The exchange offer contemplates an exchange on a par for par basis for up USD550 of new 9.00% secured notes due May 2023 upon the closing of the re-profiling and new investment or financing. The notes are expected to be secured by collateral consisting of certain intellectual property, including the Avianca brand and equity value of its aircraft fleet subject to receipt of applicable consents and approvals, if any. As of March 31, 2019, most of Avianca's USD4 billion debt was secured, excluding the 2020 bonds.

Strong Regional Market Position: Avianca's business model combines operations in Colombia, Central and South America, allowing it to rotate capacity according to market conditions. Its geographic diversification allows the company to maintain consistently solid average load factors of 82% during 2015-2018. The company's business diversification is viewed as adequate with international passengers, domestic passengers, cargo operations, and the loyalty program and other segments representing approximately 42%, 41%, 13%, and 4% of its total revenues.

Avianca's dominant position in the Colombian market is positively incorporated into the ratings. The announcement of a joint business agreement with United and Copa Airlines (not rated) should only benefit Avianca's competitive business position in the medium to long term. Regulatory approval for this transaction is expected to take approximately 12 to 18 months.

Challenge to Improve EBIT Margins: Fitch expects Avianca's EBIT margin to decrease by approximately 5.5% to 7.0% during 2019 and 2020, driven primarily by rationalization of its route network and several costs cutting initiatives. This compares with the 6.0% adjusted EBIT margin of 2018. Avianca has announced the removal of E190 aircrafts and eliminations of unprofitable routes, mainly in Peru and in selected regional markets in Colombia, while focusing on its points of network strength. Higher fuel prices and currency devaluation(s) remain as ongoing concerns. The scenario of increasing competition from smaller players in Avianca's main markets is a concern and may pressure the company's solid load factor and yield levels, as observed during 1Q19.

High Leverage to Persist: Avianca's high leverage has pressured its ratings, and the challenging operating environment in 2019 should delay any deleveraging to late 2020. Fitch expects Avianca's total adjusted leverage to improve to around 6.5x by 2020 from 6.7x in 2019. Avianca's total adjusted debt/EBITDAR was 6.6x during 2018 and 7.5x in 2017. Fitch base case does not incorporate any major non-core asset sales besides those already announced, including the Embraer's fleet.

Credit Linkages and Notes' Guarantees Structure Incorporated: The ratings also reflect Avianca's corporate

structure and credit linkage with its subsidiaries, Aerovias del Continente Americano S.A. (Avianca) and Grupo Taca. Combined, these two operating companies represent the main source of cash flow generation for the holding company. The significant legal and operational linkages between the two operating companies are reflected in the existence of cross-guarantee and cross-default clauses relating to the financing of aircraft acquisitions for both companies.

DERIVATION SUMMARY

Avianca's 'RD' rating reflects the announcement of deferred payments on certain long-term leases and principal payment on certain loan obligations. In terms of business profile, the company has a good asset base and is relatively well positioned to its regional peers based on its network, route diversification and important regional market position. Nevertheless, these factors are tempered by the company's higher gross adjusted leverage and refinancing risks, weaker liquidity and financial flexibility relative to peers.

Avianca's 'C' rating is below LATAM Airlines S.A. (LATAM, BB-/Stable) and GOL Linhas Aereas Inteligentes S.A. (GOL, B+/Stable), which have recently showed improvements in credit metrics. The ratings distinction among the three airlines reflects differences in the financial strategies, credit access, operational performance volatility and business diversification.

KEY ASSUMPTIONS

- Neutral to low single-digit yield growth;
- Load factor in the 80%-82% range;
- 2019-2020 EBIT margin moving around 5.5%-7.0%;
- Capex of USD441 million in 2019 and USD500 million in 2020.

-The recovery analysis is based on a liquidation approach given the high value of its aircraft fleet, which positively compares to the going concern approach.

-Fitch has assumed a 10% administrative claim.

Liquidation Approach:

-The liquidation estimate reflects Fitch's view of the value of aircraft and other assets that can be realized in advance rate of 70%, 75% account receivables due high percentage of credit card receivables and 50% inventories.

-These assumptions result in a recovery rate for the unsecured bonds within the 'RR5' range, which generates a one-notch downgrade to the debt rating from the IDR. Nevertheless, considering the current debt restructuring, it is commensurate with a 'C' rating level.

RATING SENSITIVITIES

Developments that May, Individually or Collectively, Lead to Positive Rating Action

- Fitch will re-rate the companies' IDRs and instruments following the completion of the exchange.
- An upgrade of the ratings for Avianca could occur following the completion of its refinancing with creditors, including the receipt of a new financing.

Developments that May, Individually or Collectively, Lead to Negative Rating Action

- Avianca's ratings will be downgraded to 'D', if the company formally files for bankruptcy protection.

LIQUIDITY

Limited Financial Flexibility: As of March 31, 2019, the company had USD357 million in cash. USD626 million of debt will come due in the short term (excluding operating leases), and USD568 million of its unsecured notes are due in May 2020. Total adjusted debt was USD5.9 billion at YE 2018. Debt consists primarily of USD4 billion of on-balance-sheet debt, most of which is secured, and an estimated USD1.9 billion of off-balance-sheet debt associated with lease obligations, per Fitch's criteria. Avianca's cash position in percentage of its LTM has deteriorated to 7.3% as March 31, 2019 from 10.3% in December 2018.

FULL LIST OF RATING ACTIONS

Fitch has downgraded and removed the following ratings from Rating Watch Negative:

Avianca Holdings S.A.

- Long-Term Foreign Currency Issuer Default Rating (IDR) to 'RD' from 'B-';

--Long-Term Local Currency IDR to 'RD' from 'B-';
--USD550 million unsecured notes due in 2020 to 'C'/RR5' from 'CCC+'/'RR5'.

Aerovias del Continente Americano S.A.

--Long-Term Foreign Currency IDR to 'RD' from 'B-';
--Long-Term Local Currency IDR to 'RD' from 'B-'.

Grupo Taca Holdings Limited

--Long-Term IDR to 'RD' from 'B-'.

Avianca Holdings, Grupo Taca, and Avianca Leasing are co-issuers of the USD550 million unsecured notes.

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Additional information is available on www.fitchratings.com

Applicable Criteria

Corporate Rating Criteria (pub. 19 Feb 2019)

Corporates Notching and Recovery Ratings Criteria (pub. 23 Mar 2018)

National Scale Ratings Criteria (pub. 18 Jul 2018)

Parent and Subsidiary Rating Linkage (pub. 16 Jul 2018)

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